

EBS/83/67  
Supplement 1

CONFIDENTIAL

April 15, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Zambia - Staff Report for the 1982 Article IV Consultation  
and Request for Stand-By Arrangement

The attached supplement to the staff report for the 1982 Article IV consultation with Zambia and its request for a stand-by arrangement has been prepared on the basis of additional information.

This subject, together with the paper on a request expected to be received from Zambia for a purchase under the compensatory financing facility (EBS/83/70, 3/31/83), has been scheduled for discussion on Monday, April 18, 1983.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

ZAMBIA

Staff Report for the 1982 Article IV Consultation and  
Request for Stand-By Arrangement--Supplementary Information

Prepared by the African Department and the Exchange  
and Trade Relations Department

Approved by O.B. Makalou and S. Kanesa-Thasan

April 14, 1983

On April 11, 1983, the following telex from the Governor of the Bank of Zambia, Mr. B.R. Kuwani, was received proposing a revision in Attachment II of the Memorandum on the Economic and Financial Policies of Zambia, which is appended to EBS/83/67.

With reference to the letter of Prime Minister Mundia dated February 25, 1983 to the Managing Director, I propose that in Attachment II to the Memorandum the month of April be replaced by May, and that footnote 5 be deleted.

The revision changes the first date of the performance criterion on the reduction of external commercial payments arrears from end-April to end-May, 1983 on account of the delay of the disbursement in respect of an expected request by Zambia for a further purchase under the Compensatory Financing Facility circulated in EBS/83/70. Accordingly, Table 1 (page 2), Table 12 (page 30), and Attachment II of Appendix II (page 53) in EBS/83/67 have been revised, as well as the proposed decision (page 35) on the stand-by arrangement and paragraph 4(a)(i) (page 36) of the proposed stand-by arrangement for consideration by the Executive Board; revised pages are attached.

## I. Introduction

The 1982 Article IV consultation discussions with Zambia were held in Lusaka during the periods November 8-23, 1982 and January 31-February 10, 1983. The Zambian representatives included Mr. N. Mundia, Prime Minister, and Minister of Finance since January 13, 1983; Mr. B.R. Kuwani, Governor of the Bank of Zambia; and other senior officials concerned with economic and financial matters. The mission head also met with President Kenneth Kaunda. The staff representatives were Messrs. E.L. Bornemann (head), W.J. Shields (both of AFR), W. Mahler (FAD), U. Gunjal (AFR), T. Hatayama (ETR), and Mrs. C. Smith and Miss M. Duane (secretaries-AFR). Mr. N. Sangare, Executive Director, participated in some of the discussions during the first mission.

Concurrently, discussions were held with the Zambian authorities on a stabilization program covering the year 1983. In the attached letter dated February 25, 1983, the Zambian Government requests a one-year stand-by arrangement in the amount of SDR 211.5 million (100 per cent of quota) in support of this program; this request and the accompanying Memorandum on the Economic and Financial Policies of Zambia are set out in Appendix II. Of the amount of SDR 211.5 million requested under the stand-by arrangement, SDR 70.9 million would be from the Fund's ordinary resources and SDR 140.6 million from borrowed resources. As of February 28, 1983, the Fund's total holdings of Zambian kwacha amounted to SDR 758.4 million, or 358.6 per cent of quota. Purchases scheduled under the stand-by arrangement and the concurrent CF request, together with repurchases scheduled during the program period, are set out in Table 1. If the full amount of the stand-by arrangement is purchased, the Fund's total holdings of Zambia's currency would rise to SDR 963.4 million at the end of March 1984, or 455.5 per cent of the present quota. Zambia's new quota will be SDR 270.3 million. A waiver of the limitation in Article V, Section 3(b)(iii) of the Articles of Agreement will be required.

The last Article IV consultation discussions with Zambia were held in Lusaka during the period August 5-17, 1981. The staff report (SM/81/196) and the report on recent economic developments (SM/81/208) were considered by the Executive Board on November 18, 1981. A summary of Zambia's relations with the Fund is provided in Appendix III. A summary of Zambia's relations with the World Bank Group is provided in Appendix IV. Zambia continues to avail itself of the transitional arrangements of Article XIV.

## II. Background to the Discussions

Zambia's economic performance in recent years has been unsatisfactory. Real GDP declined over the five-year period 1977-81 at an average annual rate of almost 2 per cent (Table 2), with the consequence that real per

Table 1. Zambia: Schedule of Proposed Purchases and Repurchases, 1983-84

(In millions of SDRs)

	1983				1984
	April	May- June	July- Sept.	Oct.- Dec.	Jan.- March
<u>Purchases</u>					
Stand-by arrangement	31.5	45.0 1/	45.0	45.0	45.0
Ordinary resources	19.1	20.4	20.5	7.8	--
Borrowed resources	12.4	24.6	24.5	37.2	45.0
CFF	--	97.2	--	--	--
<u>Repurchases</u>					
Credit tranches	3.1	25.0	25.0	21.9	18.8
CFF	--	6.1	--	--	--
Oil	--	0.7	--	--	--
<u>Net purchases</u>	28.4	110.4	20.0	23.1	26.2
<u>Total Fund holdings of Zambia kwacha (cumulative)</u>					
In millions of SDRs	783.7	894.1	914.1	937.2	963.4
As per cent of quota	370.5	422.6	432.2	443.1	455.5

Source: IMF, Treasurer's Department.

1/ Based on April and May performance criteria and satisfactory completion of the review of the program with the Fund by end-June 1983.

almost SDR 800 million by 1986, with the debt service ratio declining only modestly over the period from 53.3 per cent in 1983 to a projected 47.1 per cent in 1986. Continuing debt service obligations of this magnitude will place a severe strain on Zambia's balance of payments, even after allowing for the projected increase in export receipts and continuing restraint on imports. The estimated debt relief in 1983 is expected to reduce the debt service ratio in that year to 36 per cent. It is likely, therefore, that Zambia will need to seek further debt relief after 1983, in order to mitigate the effects on the balance of payments of the large debt service payments.

#### 7. Performance criteria and review

The proposed stand-by arrangement includes as performance criteria ceilings on net domestic assets, net credit to the Government (both of the banking system), Bank of Zambia credit to the mining company (ZCCM), external commercial payments arrears, and the contracting or guaranteeing of new nonconcessional debt in the maturity range of 1-10 years, as specified in Table 12. The ceilings for June, September, and December are indicative and will be reviewed during a mid-term review in the light of the effects of debt rescheduling on the budget and the balance of payments, actual and prospective copper prices, and the seasonal credit needs of the agricultural sector on the basis of the 1983 agricultural crop. The usual performance criteria relating to the exchange and payments system will apply.

As mentioned above, there will be a comprehensive review of progress with the Fund under the program by end-June 1983, and prior to the purchase based on the April ceilings. In particular, this review will require understandings to be reached with the Fund on performance criteria for the remaining period of the program, as well as on exchange rate and interest rate policies. Other topics of the review will include progress on debt rescheduling, budgetary performance, credit policies, and prices and incomes policies.

#### 8. Relations with the World Bank

Over the past years the Bank has been extending a number of IBRD loans and IDA credits to different economic sectors within Zambia; the current status of these loans and credits is shown in Appendix IV. More recently, the Bank and the Zambian Government have reached agreement on a Memorandum on Development Objectives and Policies, which sets out a framework for structural adjustment over the next several years. Within this framework, the Bank is assisting the Government with a number of detailed studies, including a forward budgeting study (with Fund technical assistance), an

Table 12. Zambia: Quantitative Performance Criteria for 1983 1/  
(End of period, except as otherwise specified)

	<u>1982</u> Prov. actual	<u>1983</u> April	June <u>2/</u>	Sept. <u>2/</u>	Dec. <u>2/</u>
(In millions of kwacha)					
Net domestic assets of banking system	2,859.9	2,990.8	3,045.8	3,115.8	3,170.8
Net claims on Government of banking system	1,950.3	2,025.3	2,055.3	2,075.3	2,100.3
Bank of Zambia credit to ZCCM	160.5	170.5 <u>3/</u>	170.5	165.5	160.5
(In millions of SDRs)					
External commercial payments arrears <u>4/</u>	669.3	669.3 <u>5/</u>	589.3	579.3	569.3
New external borrowing contracted or guaranteed by the Government (cumulative):					
1-10 years maturity	...				100
1-5 years maturity	...				--

Source: Appendix II.

1/ For precise definitions see Attachments I and II to Appendix II.

2/ Indicative and subject to review by mid-1983.

3/ Estimated actual.

4/ Incorporates a minimum cash reduction of SDR 30 million and a reduction through debt relief of SDR 70 million assumed to be implemented by end-June but subject to the review of progress on debt rescheduling.

5/ End-May.

### Proposed Decisions

In view of the foregoing, the following draft decisions are proposed for adoption by the Executive Board:

#### I. 1982 Consultation

1. The Fund takes this decision relating to Zambia's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1982 Article XIV consultation with Zambia, in the light of the 1982 Article IV consultation with Zambia conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Zambia's exchange system remains highly restrictive. In the context of the program supported by a stand-by arrangement, the authorities intend to pursue the policies that will permit a progressive reduction in payments arrears and facilitate other steps toward a more liberal exchange system. In the circumstances of Zambia, the Fund grants approval for the restrictions on making of payments and transfers for current international transactions referred to in SM/83/50 until June 30, 1984, or the next Article IV consultation, whichever is the earlier. The existing multiple currency practice, resulting from the levy on the sale of foreign exchange for private overseas travel, is approved until the completion of the mid-term review of the stand-by arrangement.

#### II. Stand-By Arrangement

1. The Government of Zambia has requested a stand-by arrangement in an amount equivalent to SDR 211.5 million for a period of 12 months beginning April \_\_, 1983.

2. The Fund approves the stand-by arrangement attached to EBS/83/67, Supplement 1.

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

ZAMBIA - Stand-By Arrangement

Attached hereto is a letter and annexed Memorandum dated February 25, 1983 from the Prime Minister and Minister of Finance of Zambia requesting a stand-by arrangement and setting forth: (a) the policies and objectives that the authorities of Zambia intend to pursue for the period of this stand-by arrangement; and (b) understandings of Zambia with the Fund regarding a review that will be made of progress in realizing the objectives of the program and of the policies and measures that the authorities of Zambia will pursue for the remaining period of this stand-by arrangement.

To support these objectives and policies, the International Monetary Fund grants this stand-by arrangement in accordance with the following provisions:

1. For a period of 12 months from 1983, Zambia will have the right to make purchases from the Fund in an amount equivalent to SDR 211.5 million, subject to paragraphs 2, 3, 4, and 5 below, without further review by the Fund.
2. (a) Purchases under this arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 31.5 million until June 15, 1983, SDR 76.5 million until August 15, 1983, SDR 121.5 million until November 15, 1983, and SDR 166.5 million until February 15, 1984.  
  
(b) None of the limits in (a) above shall apply to a purchase under this stand-by arrangement that would not increase the Fund's holdings of Zambia's currency in the credit tranches beyond 25 per cent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 per cent of quota.
3. Purchases under this stand-by arrangement shall be made from ordinary resources until purchases reach the equivalent of SDR 8,780,728, then from ordinary and borrowed resources in the ratio of 1:1.2, until purchases under this arrangement reach the equivalent of SDR 138,557,813; and then from borrowed resources only provided that any modification by the Fund of the proportions of ordinary and borrowed resources shall apply to amounts that may be purchased after the date of modification.
4. Zambia will not make purchases under this stand-by arrangement that would increase the Fund's holdings of Zambia's currency in the credit tranches beyond 25 per cent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 per cent of quota:

(a) During any period in which the data at the end of the preceding period indicate that

(i) the target for reduction in external payments arrears described in paragraph 19 and Attachment II of the annexed Memorandum as revised by the telex from the Governor of the Bank of Zambia of April 11, 1983, or



Zambia: Proposed Timetable for Reduction of External Commercial  
 Payments Arrears in 1983 1/

(In millions of SDRs)

	<u>1982</u> Dec. <u>2/</u>	<u>1983 Projection 3/</u> May June Sept. Dec.
Minimum cash reduction	--	10.0 10.0 10.0
Estimated reduction through rescheduling <u>4/</u>	--	70.0 -- --
Total reduction (cumulative)	--	80.0 90.0 100.0
Limits on external commercial payments arrears outstand- ing <u>4/</u> (end of period)	669.3	669.3 589.3 579.3 569.3

1/ As recorded by the Bank of Zambia as "Deposits in Forex Arrears"  
 (Forex Requirements), including overdrawn amounts in respect of letters of  
 credit and suppliers' credits not covered by a local currency deposit.

2/ SDR/K = 0.976311.

3/ SDR/K = 0.781049.

4/ Limits for June, September and December are indicative and subject to  
 review following debt rescheduling which is presently assumed to be concluded  
 by June 30.

Zambia: Relations with the Fund  
(On February 28, 1983)

Date of membership	September 23, 1965
Quota:	SDR 211.5 million
Status:	Article XIV
Exchange system:	The Zambian kwacha is pegged to the SDR, with the present rate of K 1 = SDR 0.781049 having been maintained since January 7, 1983. The U.S. dollar is the intervention currency, and the Bank of Zambia's rates for the U.S. dollar are based on the U.S. dollar/SDR rate calculated by the Fund for the preceding day.
Fund holdings of Zambian kwacha:	SDR 758.4 million, or 358.6 per cent of quota, of which SDR 146.8 million (69.4 per cent) is under the credit tranches, SDR 99.4 million (47.0 per cent) under the CFF, SDR 0.7 million (0.3 per cent) under the oil facility, SDR 77 million (36.4 per cent) under the EFF, and SDR 223 million (105.4 per cent) under the Enlarged Access Policy.
SDR position:	Holdings are SDR 8,137 or 0.0 per cent of net cumulative allocation (SDR 68.3 million).
Gold distribution (four distributions):	65,043.532 fine ounces
Direct distribution of profits from gold sales (July 1, 1976-July 31, 1980):	US\$12.07 million
Trust Fund Loan Disbursement (second period):	SDR 42.77 million
Technical assistance:	The Central Banking Department is currently providing a research advisor and an advisor to the Governor of the Bank of Zambia.
Staff contacts:	The 1982 Article IV consultation discussions were held in Lusaka in November 1982 and January-February 1983. Use of Fund resources missions visited Zambia in December 1981, April and November 1982, and February 1983. Zambian delegations held discussions at the Fund in January and September 1982.